

**IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA**

CHRISTINE C. SCHUBERT,	:	CIVIL ACTION
Trustee of the Bankrupt	:	
Estate of DAVID ALICEA,	:	
Plaintiff,	:	
	:	
v.	:	
	:	
AMERICAN INDEPENDENT	:	
INSURANCE COMPANY,	:	
Defendant.	:	NO. 02-6917
	:	
	:	

OPINION AND ORDER

Newcomer, S.J.

June , 2003

Currently before the Court are the Parties' Cross Motions for Summary Judgment. For the following reasons, both Motions shall be denied.

I. Facts and Procedure

This is an excess-verdict bad faith insurance case. The underlying verdict that led to this case arose from a car accident between David Alicea and Katrina and John Kubala. On May 11, 1997, Mr. Alicea ran a stop sign and collided with the passenger side of the car belonging to John and Catrina Kubala. Ms. Kubala was seated in the passenger side of the car and Mr. Kubala was driving. Ms. Kubala sustained serious physical injuries from the crash.

The Kubalas retained Attorney Mike McDonald to represent them involving any claims against Mr. Alicea arising

from the accident. At the time of the accident, Mr. Alicea was insured by the Defendant under a motor vehicle liability insurance policy up to the amount of \$15,000. On February 4, 1998, Mr. McDonald sent the Defendant the medical records Ms. Kubala had accumulated since the accident. The bills enclosed in these records amounted to \$41,000. In the correspondence attached to these records, Mr. McDonald asked to be advised as to Defendant's position regarding settlement. The Defendant did not make any offer to settle at that time. Instead, on March 13, 1998, the Defendant requested that Ms. Kubala undergo an independent medical examination ("IME"). On August 12, 1998, Mr. McDonald sent a letter to Defendant refusing the request for an IME, enclosing additional records, and making an offer to settle the case for the \$15,000 policy limit. The letter also stated that the offer would remain open until September 15, 1998, and that after that date the Kubalas would proceed to trial without any further negotiations within the policy limits. On September 14, the Defendant advised Mr. McDonald that it still required an IME. Later that day, Mr. McDonald again stated his position that an IME was unreasonable. The next day the policy limit offer expired without a settlement. At no time during these "negotiations" did the Defendant make its insured, David Alicea, aware of any efforts to settle the case.

In April of 1999, the Kubalas filed suit against Mr.

Alicea in the Court of Common Pleas of Lancaster County. During discovery, an IME of Ms. Kubala was performed. After receiving the results of the IME, the Defendant offered Mr. McDonald the \$15,000 policy limit. That offer was rejected. The case proceeded to trial and on August 31, 2000, a non-jury verdict was rendered in favor of Mrs. Kubala in the amount of \$2,505,755 and in favor of Mr. Kubala in the amount of \$100,000 for loss of consortium.

Following the verdict, Mr. Alicea filed for bankruptcy. The trustee of Mr. Alicea's bankruptcy estate, Christine Shubert, has brought this action on behalf of the estate, alleging that the Defendant acted in bad faith by refusing to settle the Kubala action within the policy limits. Mrs. Shubert has brought claims for breach of contract and violations of the Pennsylvania Bad Faith Insurance Law, 42 Pa. C. S. §8371.¹

II. Discussion

A. Standard for Summary Judgment

Summary judgment is appropriate only "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." FED. R. CIV. P.

¹For a more complete description of the facts surrounding the bankruptcy filing, see this Court's Order Dated May 22, 2003, Dismissing the Defendant's Counterclaim.

56(c) (1994). A genuine issue is one in which the evidence is such that a reasonable factfinder could return a verdict for the nonmoving party. See Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986). When deciding a motion for summary judgment, a court must draw all reasonable inferences in the light most favorable to the non-movant. See Biq Apple BMW, Inc. v. BMW of N. Am., Inc., 974 F.2d 1358, 1363 (3d Cir. 1992).

B. The Common Law Excess-Verdict Bad Faith Claim

1. An Excess-Verdict Bad Faith Claim Sounds in Contract

Before discussing the merits of the parties' motions, the Court will clarify the underpinnings of a excess-verdict bad faith cause of action. The right to bring an excess-verdict bad faith case against an insurance company was established by Cowden v. Aetna, 389 Pa. 459 (1957). Cowden found that

"an insurer against public liability for personal injury may be liable for the entire amount of the judgment secured by a third party against the insured regardless of any limitation in the policy, if the insurer's handling of the claim, including a failure to accept a proffered settlement, was done in such a manner as to evidence bad faith on the part of the insurer in the discharge of its contractual duty."

Id. at 468 (emphasis added). This rule is founded upon the nature of a liability insurance contract. Id. at 469. Specifically, that such contracts vest the insurer with control over litigation that can

expose the insured to personal liability. Id. Cowden thus established an implied duty to act in good faith during the defense of an insured.² See Diamon v. Penn Mut. Fire Ins. Co., 247 Pa. Super. 534, 552 (1977)(finding implied duty of good faith in an insurance contract). Thus, an excess-verdict bad faith claim is in the nature of a breach of contract. Birth Center v. St. Paul Cos., Inc., 567 Pa. 386, 402 at nt. 12 (citing Johnson v. Beane, 541 Pa. 449, 458 (1995)(Cappy, J., concurring)); Haugh v. Allstate Ins. Co., 332 F.3d 227, 236-7 (3d Cir. 2003).

2. The Standard Governing Whether an Insurer Breached its Contractual Duty of Good Faith

As this Court held in its Order of January 29, 2003, an insurer must act with due care when handling an insured's litigation. Included within this duty is the obligation to act reasonably when deciding whether or not to accept a settlement offer. Reasonableness has traditionally been the standard governing an insurer's decision whether to settle. See Cowden, at 469 (approving negligence as a ground for recovery); See, also, Geodeon v. State Farm Mutual Automobile Ins. Co., 410 Pa. 55, 59 (1963)(stating that an insurer is derelict in its duty when it, inter alia, unreasonably refuses an offer of settlement); Gray v. Nationwide Mutal Ins. Co., 422 Pa. 500, 504 (1966) (citing the

²An implied duty of good faith, is now considered an accepted part of all contracts in Pennsylvania. See Fremont v. E.I. DuPont DeNemours & Co., 988 F.Supp. 870 (E.D. Pa. 1997); RESTATEMENT OF CONTRACTS (SECOND) § 205 (1981).

above language in Geodon); Clark v. Interstate National Corp., 486 F.Supp. 145 (E.D. Pa. 1980). An insurer has been deemed to act reasonably when its decision whether or not to settle is "honest, intelligent, and objective." United States Fire Ins. Co. v. Royal Ins. Co., 759 F.2d 306, 310 (3d Cir. 1985)(citing Shearer v. Reed, 286 Pa. Super. 188, 193-4 (1981)).

3. The Reasonableness of the Defendant's Refusal to Settle for the Policy Limits Before an IME Should be Decided by a Jury

This case boils down to two mutually exclusive propositions. The first is that failing to accept the proposed offer to settle based on the medical documentation provided to the Defendant was unreasonable, and thus, the Defendant's refusal to accept the offer was in bad faith. The second is that requiring that an IME be performed before accepting any offer to settle is a reasonable stance on the part of the Defendant, and accordingly, it is not liable for the excess verdict under Cowden.

Simply because these propositions are mutually exclusive and the facts surrounding the Defendant's decision are undisputed, does not mandate the granting of a summary judgment motion. Summary judgment is only proper, both when the facts are undisputed and only one conclusion can be drawn from them. Gans v. Mundy, 762 F.2d 338 (3d Cir. 1985). In this case, a reasonable jury could find that either of the two propositions discussed above is correct. Accordingly, summary judgment should not be granted.

4. The Defendant's Failure to Inform Mr. Alicea of the Plaintiff's Offer to Settle for the Policy Limits does not Establish Bad Faith under Cowden

The Plaintiff argues that the Defendant's failure to inform Mr. Alicea of the pending offer to settle warrants a grant of summary judgment in its favor. This argument is flawed for two reasons. First, an excess-verdict bad faith case under Cowden, centers on the decision to not settle the case. If the Defendant's eventual decision to not accept the policy limit offer before obtaining an IME was reasonable, then the failure to inform Mr. Alicea of the offer could not subject the Defendant to liability under Cowden. While the failure to inform an insured of an offer to settle may be evidence of whether the Defendant had the insured's interests in mind, it is does not constitute bad faith per se. See Haugh, at 32 (noting that failure to advise insured of offer to settle could constitute evidence of bad faith).

The Plaintiff's argument is also not maintainable because there are not sufficient facts in the record to conclude that the Defendant's failure to inform Mr. Alicea of the policy limit offer caused the excess verdict. A bad faith claim under Cowden requires proof that the Defendant's conduct proximately caused the insured's damages. Builders Square, Inc. v. Jos. J. Saraca Builder Square, Inc., 1996 U.S. Dist. LEXIS 19444 (E.D. Pa. 1996). In this case, the excess verdict was caused by the Defendant's rejection of the

settlement offer. The Court is not persuaded by the Plaintiff's hypothetical situations, wherein Mr. Alicea's learning of the settlement offer would have changed the insurance company's decision not to settle the case. It is highly unlikely that an insured could ever convince an insurer to settle a case within its policy limits, and it is certainly beyond the scope of this motion for the Court to transpose such a situation onto these facts.

C. The Statutory Bad Faith Claims under § 8371

1. Section 8371 Creates a Separate Cause of Action

Both parties argue that even if they are not entitled to summary judgment on the Cowden claim, the Court should grant judgment on the statutory bad faith claim under § 8371. Before the Court can make this decision, however, it first must determine if § 8371 creates an independent cause of action under Pennsylvania law or whether it merely adds additional remedies to already accepted common law breach of contract "bad faith" actions.

After reviewing the case law in this area, the Court is convinced that there is a consensus among both federal and state Courts that § 8371 creates an independent cause of action.³ Numerous cases have held that it was the legislature's intent to create such a claim when it adopted § 8371. See, e.g., Winterberg

³There is at least one case that finds that a § 8371 claim is contingent on the success of the underlying breach of contract action. See Pizzini v. American International Specialty Lines Ins. Co., 249 F.Supp.2d 569 (E.D. Pa. 2003). Further, the Pennsylvania Supreme Court has explicitly withheld judgment on this issue. Birth Center, 567 Pa. at 403, nt. 14. The Court notes that if there is no independent cause of action under § 8371, then the refusal to grant summary judgment on this claim would be correct because summary judgment was not proper on the necessary predicate breach of contract claim.

v. Transportation Ins. Co., 72 F.3d 318, 326 (3d Cir. 1995); Nealy v. State Farm Mutual Life Ins. Co., 695 A.2d 790, 793 (Pa. Super. 1996); Romano v. Nationwide Mutual Fire Insurance Co., 435 Pa. Super. 545, 553 (1994); March v. Paradise Mutual Insurance Co., 435 Pa. Super. 597, 599 (1994). Courts have further held that a statutory claim under § 8371 can be maintained even before a contract claim has fully developed, and that a statutory claim can be successful even if the underlying breach of contract claim fails. Doylestown Elec. Supply Co. v. Maryland Cas. Ins. Co., 942 F. Supp. 1018, 1020 (E.D. Pa. 1996) (insured may bring bad faith claim prior to resolution of contract dispute); March, 646 A.2d at 1256 (insured's claim for bad faith is "independent of the resolution of the underlying contract claim"). Accordingly, the Court is free to grant summary judgment on the statutory claim irrespective of the fact that summary judgment is not proper on the Cowden claim.

2. Section 8371 should be Applied to Third-Party Bad Faith Cases

The Defendant argues that § 8371 should not be applied to cases involving bad faith conduct on the part of insurance companies which result in excess verdicts against their insured. The Defendant claims that § 8371 applies only to cases where an insurance company acts in bad faith in the handling of a claim made directly by its insured. While acknowledging that two recent cases, Birth Center and Haugh, have both applied § 8371 to excess-

verdict cases, the Defendant claims that its applicability was not raised in those cases, and thus, this Court is free to hold that § 8371 does not apply to this action.

The Court finds that the language of the statute makes it clearly applicable to the case at bar. The remedies outlined in §8371 apply to "action[s] arising under an insurance policy." 42 Pa. C. S. § 8371. As stated in Cowden, the duty to maintain the defense of an insured in good faith is a "contractual duty." Cowden 389 Pa. at 468. Thus, an excess-verdict bad faith case clearly arises from an insurance contract. See Frazier v. State Farm Auto. Ins. Co., 33 Pa. D. & C. 4th 170, 175 (C.C.P. Philadelphia 1996) (finding that plain language of § 8371 dictates that it should apply to bad faith failures to settle).

The Court cannot accept the Defendant's argument that third-party insurance claims, meaning those where the insurance contract requires payment to a party other than the insured, are fundamentally different for purposes of the § 8371 from first-party claims, in which an insurance contract mandates payment directly to the insured. In Berks Mutual Leasing Corp. v. Travelers Property Casualty, 2002 U.S. Dist. LEXIS 23749 (E.D. Pa. filed Dec. 9, 2002), Judge Yohn examined the language, history, and cases interpreting § 8371. Id. at *18. Judge Yohn concluded that § 8371 applies to causes of action arising out of the handling of a claim or benefit without distinguishing between third-party and first-party claims. Id. An unreasonable failure to settle involves the

handling of a claim. See Cowden, 389 Pa. at 468. Therefore, acting with bad faith when deciding whether or not to settle should be treated the same as the mishandling of any other claim under any other insurance contract. Accepting the Defendant's argument would categorically exclude an entire group of contracts and claims from the purview of § 8371, without any statutory language or explicit legislative intent to support the exception.⁴ The Court sees no basis on which to draw this distinction. Consequently, the Defendant's Motion for Summary Judgment on the § 8371 claim must be denied.

3. The Defendant's Conduct Does not Satisfy the Standard for a Claim under § 8371 as a Matter of Law.

Neither the Defendant's decision not to accept Plaintiff's policy limits offer to settle the claim, nor its failure to inform Mr. Alicea of the outstanding offer to settle establish a violation of § 8371 as a matter of law. A successful

⁴The entire text of § 8371 provides:

In an action arising under an insurance policy, if the court finds that the insurer has acted in bad faith toward the insured, the court may take all of the following actions:

- (1) Award interest on the amount of the claim from the date the claim was made by the insured in an amount equal to the prime rate of interest plus 3%,
- (2) Award punitive damages against the insurer,
- (3) Assess court costs and attorney fees against the insurer.

42 Pa. C. S. § 8371. The Defendant argues that the delay remedy in subsection (1) of the statute is inconsistent with third-party bad faith actions. However, the use of the word "may," clearly conveys that the legislature intended for Courts to decide which remedies should be applied in individual cases. Therefore, merely because the one remedy could not be used in a certain types of cases does not show an intent to exclude those cases from the purview of the statute.

claim under § 8371 requires two elements, 1) that the Defendant did not have a reasonable basis for not satisfying the claim, and 2) that the Defendant knew or recklessly disregarded its lack of a reasonable basis. Terlestsky v. Prudential Prop. & Cas. Ins. Co., 437 Pa. Super. 108 (1994). As discussed above, the reasonableness of the Defendant's refusal to settle the claim and pay the \$15,000 benefit under the policy is a jury question. Therefore, summary judgment based on the Defendant's refusal to settle is inappropriate.

The Defendant's refusal to inform Mr. Alicea about the offer to settle cannot be a basis for summary judgment. A § 8371 claim only arises when the an insurer actually refuses to pay some benefit due under the policy. If the refusal to pay a benefit is reasonable, other breaches of duty to the insured are inconsequential. See Hyde Athletic Indus. v. Continental Cas. Co., 969 F.Supp. 289 (E.D. Pa. 1997)(finding that because there was no duty to cover the claim, a failure to properly investigate the claim could not be a violation of § 8371). Accordingly, if the refusal of the policy limit offer was reasonable, the Defendant's failure to inform Mr. Alicea would not give him a right to recovery under § 8371.

III. Conclusion

For the above stated reasons both parties' summary judgment motions will be denied. An appropriate Order will follow.

Clarence C. Newcomer, S.J.

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CHRISTINE C. SCHUBERT,	:	CIVIL ACTION
Trustee of the Bankrupt	:	
Estate of DAVID ALICEA,	:	
Plaintiff,	:	
	:	
v.	:	
	:	
AMERICAN INDEPENDENT	:	
INSURANCE COMPANY,	:	
Defendant.	:	NO. 02-6917
	:	
	:	

O R D E R

AND NOW, this day of June, 2003, upon consideration of the Parties' Cross-Motions for Summary Judgment (Docket Nos. 27 and 38), and the responses thereto, it is hereby ORDERED that said Motions are DENIED.

AND IT IS SO ORDERED.

Clarence C. Newcomer, S.J.